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ABSTRACT

In June 1995, the U.S. Department of Education issued an audit guide that required that all institutions participating in Title IV programs have an annual compliance audit. This guide contains a notice to institutions and third party servicers that, to the extent that an institution contracts with a server to administer any aspect of Title IV programs, the applicable compliance requirements also apply to the server. This document also contains an update to the 1995 Audit Guide that provides guidance to the independent public accountants engaged to audit functions performed by institutions servers, identifies additional compliance requirements, clarifies some existing requirements, and includes information on changes that result from regulations effective as of July 1, 1997. Some portions of the guide update are pages to be inserted into the original; other sections contain pen-and-ink changes to be inserted. (SLD)

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AUDIT GUIDE

ED 459 640

COMPLIANCE AUDITS (ATTESTATION ENGAGEMENTS) OF FEDERAL STUDENT FINANCIAL ASSISTANCE PROGRAMS AT PARTICIPATING INSTITUTIONS AND INSTITUTION SERVICERS

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U.S. DEPARTMENT OF EDUCATION
OFFICE OF INSPECTOR GENERAL

JULY 1997 UPDATE

HED345528

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UNITED STATES DEPARTMENT OF EDUCATION

OFFICE OF INSPECTOR GENERAL

THE INSPECTOR GENERAL

July, 1997

OIG-97-1

Dear Colleague:

In June 1995, we transmitted by Dear Colleague letter the U.S. Department of Education's (ED) Audit Guide, *Compliance Audits (Attestation Engagements) of the Federal Student Financial Assistance Programs at Participating Institutions* (Guide). That Guide required all institutions participating in Title IV HEA Programs to have an annual compliance audit, and applied to award years ending June 30, 1995, and thereafter. This letter serves as notice to institutions and third party servicers that, to the extent that an institution contracts with a servicer to administer any aspect of the Title IV HEA Programs, the applicable compliance requirements contained in the Guide also apply to that servicer.

Accompanying this letter is an update to the Guide that provides guidance to independent public accountants (IPA) engaged to audit functions performed by institution servicers when the functions performed are applicable to the administration of the Title IV HEA Programs, and provides guidance when auditing and reporting on a servicer's compliance with the Title IV requirements. This update also provides clarifications, identifies additional compliance requirements and management assertions applicable to institutions and institution servicers, and includes information on changes required as a result of regulations that are effective July 1, 1997. Care must be exercised to ensure that laws and regulations applicable to the audit period are being used as criteria for the determination of compliance.

Please note that audit packages submitted under this Audit Guide must contain all the components required by the Guide, including all the required elements listed on page I-13 or III-7 and 8 of the Guide, as applicable. Audit packages submitted without all the required components are incomplete and will be rejected and returned to the institution or servicer. Institutions and servicers that do not submit a complete audit in accordance with the Audit Guide may be subject to administrative sanctions pursuant to 34 CFR 668 Subpart G.

This update consists of a list of changes to be made by pen and ink as well as new and revised pages to be inserted to the Guide. In lieu of making the pen and ink changes and inserting new pages and sections, an updated version of the audit guide (SFA Audit Guide-Updated 1997) with these changes already inserted is available on the Internet at this URL: http://home.gvi.net/~edoig/. The Guide as amended by this update must be used by the IPA for performing the compliance audits of any institution or institution servicer participating in or administering any aspect of Title IV HEA Programs, except for institution or institution servicers which obtain an audit in accordance with the Office of Management and Budget Circulars A-128 or A-133.

Questions pertaining to the Guide and update should be faxed directly to the Non-Federal Audit Team at (214) 767-2024. We look forward to working with you to implement the compliance audit requirements for Title IV HEA program institutions and institution servicers.

Sincerely,

Thomas R. Bloom

Enclosure

JUNE 1995 SFA AUDIT GUIDE CHANGES

The following are changes that must be made to several pages of the June 1995 SFA Audit Guide. The words in *italics* are those that must be added, words with double underlines must be deleted, and the deletion and addition of paragraphs and pages are self-explanatory. After making the changes, please take a few minutes to review this information to ensure that you understand the ramifications of the changes.

Section & Page No.	
Contents	Remove pages *i* and *ii*, insert attached pages *i* through *iv*
I-1	Caption at top of the page should read: PLANNING AND OTHER CONSIDERATIONS *FOR AUDITS OF INSTITUTIONS*
I-2	Third paragraph, should read: This guide is to be used by all institutions *(including foreign schools)* which administer SFA funds, with *one exception*: *Public colleges, State and local universities, and nonprofit institutions audited in accordance with OMB Circular A-133 or its predecessors. NOTE: Organizations whose funding is below OMB Circular A-133's threshold (currently $300,000 per fiscal year) are exempt from submitting a single audit to the Department under OMB Circular A-133. The organization may be asked to submit to the Department copies of any financial statement or compliance audits that are otherwise prepared for the institution.*
I-2	Fourth paragraph should read: This guide is divided into *five* sections:
I-2	Caption, Section I should read: Sections I *and III* Caption, Section II should read: Sections II *and IV* Caption, Section III, change the III to *V*
I-3	Replace this page with attached pages I-3a, I-3b and I-3c.
I-4	Delete first two paragraphs and the address.
I-4	Auditor Qualifications, first paragraph, line 2 should read: Standards, including continuing education *and peer review* requirements. Add this paragraph at the bottom of the page under the caption Auditor Qualifications: *The IPA and audit firms must comply with the applicable provisions of the public accountancy law and rules of the country in which they*

Section & Page No.

are licensed and where the engagement is being performed. If the country does not have any public accountancy law or professional standards, the IPA must follow United States standards.

I-6 Third paragraph, second line. Delete compliance attestation and insert *audit*. Last line, delete III and insert *V*.

I-6 Fourth paragraph, first line. Delete Compliance attestation reports and insert *Audit report packages*

I-6 Last paragraph, fifth line. After the word, All, insert *institution*

I-7 Student Confirmations. First sentence should read: The IPA should consider sending positive confirmations to verify student *existence and* attendance at the institution.

I-7 Above the caption Financial Statement Audit, insert the caption ***AUDIT REPORT PACKAGE*** and this sentence: *The institution shall transmit five copies of the institution's audit report package and its corrective action plan to the address listed at the top of page I-13.*

I-7 On the caption, Financial Statement Audit, delete the word Audit and add an *"s"* to the end of the word Statement.

I-7 Insert this paragraph just prior to the caption, Management and Legal Counsel Representation Letters

Foreign institutions' financial statements may be prepared in accordance with the generally accepted accounting principles of the institution's home country if the institution administered less than $500,000 of Title IV funds during its fiscal year. Institutions administering more than $500,000 per fiscal year must have their financial statements translated into United States standards (34 CFR 668.15).

I-8 85/15 Attestation. Delete the word Attestation and insert *Revenue Test*. Delete the sentence: ED will provide guidance which will address the 85/15 attestation, which is effective July 1, 1995, and other financial statement issues. Insert a new sentence: *A proprietary institution must disclose in a footnote to its audited financial statements the percentage (including the figures used to make the calculation) of its revenues derived from the Title IV funds received during the fiscal year covered by that audit (34 CFR 668.23). The calculation must be made on a cash basis and in accordance with 34 CFR 600.5.*

Section & Page No.

I-8 Contact Office. Delete the address and telephone numbers and insert:

U. S. Department of Education
Performance Improvement and Procedures Division, IPOS
Attn: Financial Analysis
600 Independence Avenue, SW
ROB-3, Room 3682
Washington, DC 20202-5265

Tel. (202) 260-5742
Fax: (202) 708-6730

I-8 Under the caption Financial Statement Reporting, the sentence should read: An institution's financial statement *portion of the audit* report package must include the following:

I-8 Under the caption, Financial Statement Reporting, item 3. At the end of the sentence replace the semicolon with a period, delete the word and.

I-8 Bottom of page, paragraph starting Please refer...., delete entire paragraph. Insert: *The requirements for the compliance portion of the audit report package start at the bottom of page I-12.*

I-9 Top of page, delete both addresses.

I-9 Caption, Compliance Attestation Engagement, second paragraph, first line. Insert after the word in: *Section II of*

I-9 After the second paragraph under Compliance Attestation Engagement, insert this header and paragraph:

Computer and Electronically Processed Data

Because of the growth in the use of computers, institutions are processing SFA information electronically; however, the IPAs audit objectives do not change. IPAs should consider the controls over computers and the SFA information processed electronically. Some items to be considered are: Operating procedures, processing schedules, physical and internal computer security (location and accessability to terminals, controls over passwords, etc), reliability of computer processed data, computer backup schedules, and disaster recovery plans.

Section & Page No.

I-10 Fourth line of paragraph under the caption, Sampling Methodology, delete the word award and insert *fiscal.*

I-11 In the formula, replace the word award with *fiscal.*

I-11 In both Approaches, I and II, in both items, 1 and 2, replace the word award with *fiscal.*

I-12 Third line in the third paragraph under Sample Results. Delete the words, on diskette. Last sentence, delete the phrase, To download the software for Example E, and insert at the end of that sentence: *for submitting Example E.*

I-12 Following the caption, Compliance Attestation Reporting, delete the sentence and replace with: *The compliance report section of the institution's audit report package must start with a page which clearly indicates the programs, sites, and period which were examined (Example B). A complete audit report package must be mailed to:*

I-13 Address at top of the page, delete the third and fourth lines and insert: *Data Management and Analysis Division, IPOS.* Fifth line of address should read: ROB 3, Room *3522*

I-13 The sentence after the address should read: The *compliance portion of the* institution's report package must include the following:

I-13 Item 1, after the parenthetical expression, (Example C), insert: *and if the institution uses a servicer, the Servicer Information Sheet(Example C-1)*

I-13 Item 3, after the words Example E, delete the word on diskette and insert - *See Appendix D*

II-1 Start of the title, insert the word *Institution's.*

II-1 Item 2 should read: *Briefly* describes the related compliance requirements; and

II-1 First bullet, 34 CFR Parts, second line, delete July 1, 1994 and the rest of the sentence and insert: *July 1, 1996 and final regulations issued for 34 CFR Parts 668, 673, 674, 675, 676 and 690 on November 27, 1996; Parts 600 and 668 on November 29, 1996; and Parts 668, 674, 675, 676, 682, 685, and 690 on November 29, 1996.*

Section & Pag. No.

II-1 After the second bullet, ED "Dear Colleague" Letters, insert a new bullet:

The Direct Loan School Guide for the year(s) being audited.

II-1 Third indented bullet after the bullet, The institutions:, after the word Monthly insert: *Cash Summary and Data Matching*

II-1 At the bottom of the page delete the sentence: All compliance testing is based on the award year ending June 30th during the entity's fiscal year.

II-2 First bullet, delete the phrase, covering the award year.

II-2 Compliance Requirements, second indented bullet after the first bullet. Add a third bullet as follows:

Undergraduate programs offered in credit hours must meet certain requirements for the amount of instruction provided in each credit hour, unless exempted by regulation. The requirements are spelled out in 34 CFR 668.8 (k) and (l) and 668.9. Dear Colleague Letter (DCL) GEN-95-38 dated August 1995 notified institutions of the actions they must have taken to assure they were in compliance with the requirements. Note: DCL GEN-95-38 can be obtained by calling 1-800-4FEDAID or accessing the SFA electronic Bulletin Board System.

II-2 Second and third bullets. Replace the word award with *fiscal*.

II-3 Second bullet. At the end after the word, year, insert: *that ended during the institution's fiscal year.*

II-3 After the bullets but before the first full paragraph on this page insert these compliance requirements:

Published and distributed to required parties, an annual campus crime report that contains all the required information at 34 CFR 668.47.

Prepared and disseminated to all enrolled students or prospective students by mailing or appropriate publications, annual information regarding completion or graduation rates and transfer-out rates of certificate or degree-seeking full-time undergraduate students. A similar annual published report on student athletes is also required(34 CFR 668.41, 668.46 and 668.49).

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Prepared annually, for institutions offering "athletically related student aid" a compilation of revenues and expenses of intercollegiate athletic activities by specific sports which must be independently audited at least every three years and must be made available to the public (34 CFR 668.14).

II-3 Suggested Procedures, item b, 2. Change award year to *fiscal* year.

II-4 Insert after suggested procedure number 4 :

5. *If the institution offers undergraduate programs in credit hours, determine if the institution followed 34 CFR 668.8 (k) and (l) and 668.9 and DCL GEN-95-38 guidance, as applicable. Obtain, review and verify that any required clock to credit hour conversion(s) conform to requirements.*

II-4 On this page replace the term, award year, with *fiscal* year except as noted in the following change.

II-4 Suggested Procedure g should read: Obtain from the institution its calculation of its *award year* institutional eligibility ratios.

II-5 Suggested Procedure h, after this procedure insert:

i. Obtain and inspect the annual security report. Verify that the report contains all information required by 34 CFR 668.47 and was distributed as required.

j. Verify that the annual information regarding completion or graduation rates and the transfer-out rates of certificate or degree-seeking full-time undergraduate students was disseminated to all enrolled students or prospective students. Verify that the information on student athletes was published in an annual report. On a test basis, trace and verify the information.

k. If applicable, obtain and review the annual report regarding intercollegiate athletics. Verify the report revenues and expenses include all applicable sport activities and that an audit report is issued every three years.

II-6 First bullet, change the year from 1993 to *1995* and replace comma at end of sentence with a period and insert: *Note: The EDCAPS system will be replacing the PMS 272 sometime in late calendar 1997 or early 1998. There will be an EDCAPS Recipient's Guide; the IPA should review that Guide and adjust the Suggested Procedures below accordingly.*

Section & Page No.

II-6 Second bullet should read: FDLP monthly reconciliation report including (34 CFR 685.308):

Loan Detail Records,
Cash Detail Records, and
Summary Records that include totals of each type of cash and loan detail record.

II-6 Third bullet should read: SSCRs [34 CFR 682.610(c) and 34 CFR 685.308(b)]

II-6 Next paragraph, first sentence, second line. After the term, Pell awards, insert: *that were* and after the word, to, insert: *ED.*, delete the remainder of the sentence, or under-reported to the Pell Grant Financial Management Division. Next sentence after the word in, delete the word, an, and insert: *the original timely filed...* In the reference, delete (c) or (e) and insert: *and 668.23.*

II-6 Suggested Procedures, a, third bullet, delete the phrase: to guarantee agencies.

II-7 Suggested Procedure c, delete the procedure and item 1 and insert:
Obtain monthly reconciliation reports and the FDLP guidance on this subject for the audit period.

1. On a test basis determine that the institution submitted the required monthly reconciliations.

II-7 Suggested Procedure c, 2. Delete the word, cash.

II-7 Suggested Procedure c, 2, b. Delete word Servicer, insert *Loan Origination Center (LOC).*

II-7 Suggested Procedure c, 3. Renumber as *4* and insert a new procedure 3 as follows:

3. As applicable and on a test basis, determine that the data in the institution's system is reconciled to the FDLP software system.

II-7 Suggested Procedure d. After the word, of, insert *FFELP and FDLP*

Section & Page No.	
II-7	Bottom of page, Suggested Procedure e. Insert: *1.* in front of the procedure and insert: *2. Documentation supporting the Pell adjustment request must be included in the transmittal of the audit report package. Follow applicable guidance in Dear Colleague Letter GEN 94-14 or its successor*
II-9	Delete this page and insert revised pages II-9a and II-9b attached.
II-10	Ninth bullet regarding signed Statements - delete: Selective Service Registration and insert: *on Overpayments and Defaults*. The references should read: *(34 CFR 668.7 and 668.32).*
II-11	Suggested Procedures, item a, second paragraph. Add this reference at the end of the paragraph: *34 CFR 668 Subpart J, Sections 141 through 156.*
II-12	Suggested Procedures, First paragraph 3, delete and insert: *If the test is not given at an assessment center, determine if the test administrator forwards test results within two days to the test publisher for scoring.*
II-12	Suggested Procedures, Item c, 9, delete and replace with: *Has evidence of a signed FAFSA, Renewal Application, or if filed electronically, evidence of a signed "echo document."*
II-14	After the caption, Payment Periods, delete the paragraph and replace with the information on the new page II-14a.
II-14	To the right of the caption, Pell, delete the first paragraph.
II-15	Disbursement Criteria, column, **Institutions must**, first box: delete the words, 3 weeks, and insert *10 days,* in the reference delete all numbers after 34 CFR except for 668.165. Second box, delete the reference and replace with: *(34 CFR 668.164)*
II-15	First footnote under disbursement criteria box, delete the word: any, and insert an *a* in its place, delete the phrase, at that institution, at the end of the sentence.
II-16	After the end of the sentence at the top of the page insert: *Loan funds provided by electronic fund transfer or master check may not be requested earlier than: 27 days after the first day of classes of the first payment period for a first-year,*

Section & Page No.

first-time borrower; or 13 days before the first day of classes for any subsequent payment period for a first-year, first-time or for any payment period for all other FFEL borrowers. (34 CFR sections 682.603, 682.604 and 668.167).

II-16 delete the paragraph after the caption FDLP and insert the following: *The institution must determine that the student maintained continuous eligibility from the beginning of the loan period described in the promissory note. Option 1 and Option 2 institutions may not disburse loan proceeds until they have obtained a legally enforceable promissory note. Option 1 and standard origination institutions may only disburse funds for students listed on the Actual Disbursement Roster. All institutions must submit disbursement records to the loan origination center no later than 30 days following the date of disbursement. Option 1 and Option 2 institutions must also submit loan origination records and promissory notes within 30 days of the initial loan disbursement (34 CFR section 685.303 and 301).*

II-16 Suggested Procedure a, third bullet should read: *Requesting and* disbursing....

II-16 Suggested Procedure b, 1, delete words: three weeks, and insert: *10 days*.

II-17 Suggested Procedure e at top of page, delete (for Pell at institutions with nonstandard terms or clock hours).

II-17 After Suggested Procedure e at the top of the page insert:

f. Request, for FFELP loan proceeds transmitted by EFT or master check, the funds earlier than, as appropriate, the 27 and 13 day restrictions.

II-17 Suggested Procedure b should read: *Has obtained a legally enforceable FDLP promissory note;*

II-17 Suggested Procedure c, should read: *Disbursed (for FDLP Schools) loan proceeds only for students listed on the Actual Disbursement Roster (Option 1 and standard origination schools); input actual (not estimated) disbursement dates in the FDLP software system; submitted initial disbursement records, loan origination records and promissory notes to the LOC within 30 days of the initial disbursement; and all second and subsequent loan disbursement records to the LOC within 30 days of disbursement;*

Section & Page No.

II-22 Under Required Management Assertion, add:

FOR FISCAL YEARS STARTING ON OR AFTER JULY 1, 1996, THESE COMPLIANCE REQUIREMENTS MUST BE TESTED AT INSTITUTIONS THAT RECEIVED MORE THAN $300,000 OF TITLE IV FUNDING THROUGH ONE OPE ID NUMBER DURING THE FISCAL YEAR BEING AUDITED.

II-25 Contact Office. Delete the address and telephone numbers and insert:

U. S. Department of Education
Performance Improvement and Procedures Division, IPOS
Attn: Financial Analysis
600 Independence Avenue, SW
ROB-3, Room 3682
Washington, DC 20202-5265

Tel. (202) 260-5742
Fax: (202) 708-6730

II-25 After this page insert the new part 8, pages II-26 through II-29, and Sections III and IV.

SECTION III ILLUSTRATIVE REPORTS AND APPENDICES - should read *SECTION V*

Section V After the caption, Example B, delete: Report Package Cover Page and insert: *Compliance Report Section.*

After the caption, Example B, insert: *Example B-1 Servicer Cover Page*

After the caption, Example C, insert: *Example C-1 Servicer Information Sheet*

Section V After the caption, Appendix D, delete the word: Downloading.

Example B Delete caption: REPORT PACKAGE COVER PAGE and insert: COMPLIANCE REPORT SECTION

In the Note: delete the words: report cover, and insert: *page*

Section & Page No.	
Example B	Bottom of page, caption FOR THE AWARD YEAR ENDING JUNE 30, 19XX, delete the word: AWARD and insert: *FISCAL*, delete: June 30, 19XX and insert: *Month Day, Year*.
Example B	After this Example, insert Example B-1.
Example C	Page 2 of 2. Paragraph starting: The entity utilizes an SFA Servicer...., delete this paragraph as Example C-1 is required if an entity utilizes a Servicer.
Example C	After this Example, insert Example C-1.
Example D	In this Example, replace the word [Institution] with *[Institution/Servicer]*, also insert after the date, June 1995, the words *as updated*.
Appendix B	Third box under the caption, Cash Management, delete one of the words, between and after general insert the word *ledger*.
Appendix D	Delete page 1 and paragraphs 4 and 5 on page 2. Insert new page 1 attached.
Appendix D	Page 3, delete the paragraph following the caption Multiple Schools and insert:

The software program provides for data entry for multiple institutions.

Utilities Menu

This menu contains a READ ME file which provides information on how to operate the software program. IPAs are strongly encouraged to view or to print and read this information before running the software program.

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ENGAGEMENT PERIODS AND REPORT DUE DATES

Effective for reports submitted on or after July 1, 1997 the annual periods to be audited are:

- Institution's basic GAAP financial statements, based on the institution's fiscal year, in accordance with *Government Auditing Standards* and generally accepted auditing standards; and

- Compliance based on the institution's fiscal year by examining and reporting on the institution management's assertions about compliance with specified SFA laws and regulations, in accordance with SSAE No. 3 and *Government Auditing Standards*.

Institutions may engage different IPAs to perform the audit of the financial statements and the compliance attestation engagement.

A combined financial statement and compliance attestation report package is due six months following the fiscal year end as shown below. This change in the compliance audit period from an award year to a fiscal year requires *a separate compliance attestation report package* that is also due which covers the period from the date of the last compliance report (should be period ending June 30, 1995) to the end of the fiscal year prior to the first fiscal year compliance audit (34 CFR 668.23).

Institution's Fiscal Year Ending	Due Date	Financial Statement and Compliance Attestation Report Package for Fiscal Year Ending	Stub Period Compliance Attestation Report Package Covers
March 31, 1997	September 30, 1997	March 31, 1997	7/1/95 - 3/31/96
June 30, 1997	December 31, 1997	June 30, 1997	None
September 30, 1997	March 31, 1998	September 30, 1997	7/1/96 - 9/30/96
December 31, 1997	June 30, 1998	December 31, 1997	7/1/96 - 12/31/96
March 31, 1998	September 30, 1998	March 31, 1998	7/1/96 - 3/31/97
June 30, 1998	December 31, 1998	June 30, 1998	None

The institution's failure to meet report due dates may result in administrative sanctions described in 34 CFR 668, Subpart G. Questions concerning report periods and due dates should be addressed to the Performance Improvement and Procedures Division, IPOS, contact office shown on Page I-8.

MATTERS REQUIRING IMMEDIATE ACTION

Irregularities or Illegal Acts

This Guide requires practitioners to design and perform procedures to provide reasonable assurance of detecting significant illegal acts and to report directly to the ED Office of Inspector General any fraudulent act or indication of such acts. In addition, paragraph 30 of SSAE No. 3 says that an examination-level engagement includes "designing the examination to detect both intentional and unintentional noncompliance that is material to management's assertion." Accordingly, practitioners should be aware of fraud or high risk areas and recognize basic weaknesses in internal controls. See Appendix B for a list of high risk indicators or conditions a practitioner may encounter while performing the compliance engagement.

As described in Paragraph 4.16 of *Government Auditing Standards*, if the practitioner becomes aware of fraud or indications of fraud, the practitioner should exercise due professional care to avoid any actions that would compromise the protection of an individual's rights and the integrity of any official inquiries. Upon discovery of a fraudulent act or indication of such an act related to Federal programs, this Guide requires the practitioner to immediately contact the ED Office of Inspector General, Investigation Services, by phone or fax at the numbers shown below before extending audit steps and procedures. In addition, the practitioner must promptly prepare a separate written report concerning fraudulent acts or indications of such acts and include all information described in Section IV on reporting findings. This report should be submitted to the ED Office of Inspector General, Investigation Services, within 30 days after the date of discovery of the act or within the time frame agreed to by the practitioner and the ED Office of Inspector General, Investigation Services. The practitioner shall submit this report to the Assistant Inspector General for Investigations at this address:

Assistant Inspector General for Investigations
U. S. Department of Education
600 Independence Avenue, SW, Room 4122, MES
Washington, D.C. 20202-1510
Phone: 202-205-8762
Fax: 202-205-9449

For supplemental guidance, see Chapters 4 and 5 of *Government Auditing Standards*. In addition, practitioners may wish to consult SAS No. 53, *The Auditor's Responsibility to Detect and Report Errors or Irregularities*, SAS No. 54, *Illegal Acts by Clients* (AICPA, *Professional Standards*, vol. 1, AU sec. 317) and SAS No. 82, *Consideration of Fraud in a Financial Statement Audit*.

Due Care and Professional Skepticism

Paragraph 3.26 of *Government Auditing Standards* states that due professional care should be used in conducting the audit and in preparing related reports. Paragraph 37 of SSAE No. 3 requires that the practitioner "exercise (*a*) due care in planning, performing, and evaluating the results of his or her examination procedures and (*b*) the proper degree of professional skepticism to achieve reasonable assurance that material noncompliance will be detected." This Guide cautions practitioners against ignoring basic weaknesses in internal controls, performing audit steps mechanically (auditing form over substance), and accepting explanations for audit exceptions without question.

Federal Direct Loan Program (FDLP)

Eligible students or their parents may obtain a FDLP to pay for the student's cost of education. ED makes low interest loans to students and/or parents, the loans are disbursed by participating institutions. An institution may simultaneously participate in FDLP and FFELP but *a student or parent borrower may not borrow under both programs during the same period of enrollment.*

FDLP is a new program that is changing annually. You should obtain and review the institution's copy of the *Direct Loan School Guide* for the year(s) being audited. Institutions participate under one of three School Origination Options. Key concepts contained in the 1996-97 *School Guide* for each option follow.

For the 1995-96 Award Year	Level 2	Level 1	Alternative Origination
For the 1996-97 Award Year	Option 1	Option 2	Standard
Functions			
Create loan origination record	School	School	School
Transmit record to Loan Origination Center(LOC)	School	School	School
Prepare promissory note	School	School	LOC
Obtain completed/signed promissory note from borrower	School	School	LOC
Transmit promissory note to LOC	School	School	N/A
Determine funding needs	LOC	School	LOC
Initiate drawdown of funds	LOC	School	LOC
Receive funds electronically	School	School	School
Disburse loan to borrower	School	School	School
Create disbursement record	School	School	School
Transmit disbursement record to LOC	School	School	School
Reconcile on monthly basis (Data Matching)	School	School	School

The FDLP is an electronic program except for the original promissory note which is mailed to the LOC. Electronic records are created, exported (batched), and transmitted to the LOC and acknowledged (imported from) the LOC, a cycle approach. A cycle is not complete until the last activity in it is finished, i.e., an action has been accepted by the LCC and the school's system reflects the acceptance. FDLP has five types of cycles: Loan Origination Records(one for each loan), Promissory Note Manifests, Disbursement Records, Change Records and Reconcilement Records. For a loan to be "booked," the institution must have electronically transmitted to the LOC and the LOC must have accepted these records:

Loan origination record;

Promissory Note Manifest (matched with the paper promissory note sent by the school/student); and

First disbursement of loan proceeds.

Unique to FDLP : Direct Loan funds do not appear on the PMS 272;

There is no Direct Loan application, the FAFSA serves as the application.

The borrower's original accepted promissory note will not be at the institution. However, some institutions have opted to keep a copy of the note but the institution is not required to keep a copy.

Federal Perkins Loan

The Federal Perkins Loan provides loans to students. Institutions maintain a revolving loan fund started with a Federal capital contribution and a matching institutional capital contribution. Principal and interest repayments and reimbursements for canceled loans are deposited into this fund. The institution, in turn, is fully responsible for administering the program (i.e., approving, disbursing and collecting the loans).

Federal Work Study (FWS)

The FWS program provides part-time employment to needy students and is intended to broaden the range of worthwhile job opportunities for students. Students apply directly to and are selected by, the institution. The institution determines the award amount, job placement, and pays the student.

Payment Periods:

Effective July 1, 1997, there is a uniform definition of payment period for the Title IV programs (except for FWS) as follows:

For an eligible program that has academic terms, measures progress in credit hours, and is offered in semesters, trimesters, quarters or other academic terms, the payment period is the semester, trimester, quarter, or other academic term.

For an eligible program that measures progress in credit hours and does not have academic terms or measures progress in clock hours: (1) For a student enrolled in an eligible program that is one academic year or less in length --(i) the first payment period is the period of time in which the student completes the first half of the program as measured in credit or clock hours; and (ii) the second payment period is the period of time in which the student completes the second half of the program as measured in credit or clock hours. (2) For a student enrolled in an eligible program that is more than one academic year in length --(i) For the first academic year and any subsequent full academic year as measured in credit or clock hours --(A) the first payment period is the period of time in which the student completes the first half of the academic year as measured in credit or clock hours; and (B) the second payment period is the period of time in which the student completes the second half of that academic year; (ii) for any remaining portion of an eligible program that is more than one-half an academic year but less than a complete academic year -- (A) the first payment period is the period of time in which a student completes the first half of the remaining portion of the eligible program as measured in credit or clock hours; and (B) the second payment period is the period of time in which the student completes the remainder of the eligible program; and (iii) for any remaining portion of an eligible program that is not more than half an academic year as measured in credit or clock hours, the payment period is the remainder of the eligible program (34 CFR 668.4).

There are additional requirements on payment periods. The IPA should familiarize him or herself with the entire payment period definition.

The institution may make direct disbursements to students or credit students' accounts. If the institution credits student accounts, it must either give students receipts or notify students of the payment. Specific program requirements are:

8. PERKINS COLLECTIONS AND DUE DILIGENCE

Required Management Assertion

[Institution] complied with the Perkins Collections and Due Diligence compliance requirements listed in section II of the ED SFA Guide.

Compliance Requirements

SFA compliance requirements concerning Perkins Collections and Due Diligence are contained in 34 CFR 674. The institution must exercise due care and diligence in the collection of loans. The regulations covering the deferment of repayments of Perkins Loans are shown in 34 CFR 674.34 and .35 In addition, the deferment procedures are contained in 34 CFR 674.38. Due diligence requirements are contained in 34 CFR 674 Subpart C.

Deferment of Payments:

Payments on Federal Perkins Loans may be deferred during particular periods based on the date of the loan. The borrower need not repay principal, and interest does not accrue, except that interest does accrue during a hardship deferment for loans made before July 1, 1993. Deferments may only be granted when requested in writing and submitted to the school by its due date and with required documentation. A borrower is entitled to a 6-month grace period (post-deferment grace period) after each deferment and neither the deferment nor the grace period is included in determining the 10-year repayment period. Below is information on three types of deferments, you should review Chapter Six of *The Federal Student Financial Aid Handbook* applicable to the audit period for additional information concerning deferments.

In-school deferment;

Deferments may be given to borrowers who are regular students enrolled at least half-time in an eligible institution of higher education or a comparable institution outside the U.S. approved by ED for this purpose. It is not a requirement that the school participate in the Federal Perkins Loan Program in order for the borrower to qualify for an in-school deferment. For loans made on or after July, 1993, borrowers who are in approved graduate fellowship programs, rehabilitation training programs for disabled individuals, or are engaged in graduate or post-graduate fellowship-supported study also qualify for an in-school deferment. However, deferments may not be granted to a borrower while serving in a medical internship or residency program, except for a residency program in dentistry.

Economic Hardship Deferment;

For Federal Perkins loans made on or after July 1, 1993, a deferment of up to three years may be granted for economic hardship. To qualify, the borrower must be seeking and unable to find full-

time employment or be suffering an economic hardship. To qualify as suffering economic hardship, the borrower must provide documentation satisfactory to the institution showing economic hardship as described in 34 CFR 674.34.

Three Year Deferments;

A borrower of a Federal Perkins Loan made before July 1, 1993, may defer repayment for up to three years and interest will not accrue while the borrower is:

a member of the U.S.Army, Navy, Air Force, Marines, or coast guard;

a member of the National Guard or the reserves serving a period of full-time active duty in the Armed Forces;

an officer in the Commissioned Corps of the U.S. Public health Service;

On full-time active duty as a member of the National Oceanic and Atmospheric Administration Corps;

a Peace Corps volunteer;

a volunteer under Title I-Part A of the Domestic Service Act of 1973 (ACTION);

A full-time volunteer in service for a tax-exempt organization that ED has determined is comparable to Peace Corps or ACTION service; or

Temporarily totally disabled or unable to work because he or she must care for a *spouse or other dependent* who is so disabled.

Cancellation:

A borrower may have all or part of his or her loan (including interest) canceled for engaging in public service such as teaching or service in programs such as Head Start, Peace Corps, and ACTION, or service in the military. The borrower must apply for cancellation of the loan by obtaining the appropriate cancellation form from the business or student loan office of the school that made the loan or its servicer. The form and any required documentation must be submitted on a timely bases. The conditions which apply and the loan amounts which may be canceled vary depending on the date of the loan and the type of service performed to qualify for the cancellation. The auditor should review Chapter Six of *The Student Financial Aid Handbook* applicable to the audit period to determine the specific criteria which apply.

Billing and Collections:

Billing refers to that series of actions the school routinely performs to notify borrowers of payments due, remind them of overdue payments, and demand payment of overdue amounts. Generally, repayments begin after a grace period of either six or nine months. An "initial grace period" of nine months immediately follows a period of enrollment and immediately precedes the date repayment is required to begin for the first time. A borrower who returns to school on at least a half-time basis prior to completion of the initial grace period is entitled to a full initial grace period. The school must contact the borrower during both initial and post-deferment grace periods to remind him or her when repayment will begin. If a payment is overdue and the school has not received a request for deferment, postponement, or cancellation, the school must send the borrower an overdue notice. A first notice must be sent within 15 days after the due date, a second notice within 30 days after the first notice and a final demand sent within 15 days after the second notice. If the borrower does not respond to the final demand letter within 30 days, the school must try to make contact by telephone before beginning collection procedures.

Collection procedures are the more intensive efforts a school must make when borrowers have not responded satisfactorily to billing procedures and are considered seriously in default. The first step a school must take in the collections process is to report a defaulted loan account to a national credit bureau organization with which ED has an agreement. The second step the school must take is to use its own personnel to collect or hire a collection firm. If efforts cannot convert the account to regular repayment status within 12 months (or the borrower does not qualify for deferment, postponement, or cancellation), the school must either litigate or make a second effort to collect. The second effort to collect requires that:

> If the school first attempted to collect by using its own personnel, it must refer the account to a collection firm, unless state law prohibits it; or
>
> If the school first used a collection firm, it must use a different firm or its own personnel, or submit the account to ED for assignment.
>
> If a collection firm (retained by a school as part of its second effort to collect) cannot place an account into regular repayment status by the end of 12 months (or if the borrower does not qualify for deferment, postponement, or cancellation), the firm must return the account to the school.

The school must continue to make annual attempts to collect the account until:

> the loan is recovered through litigation;
>
> the account is assigned to ED; or
>
> the loan is written off.

The school must assess all reasonable collection costs against the borrower, without regard to the provisions of state law. The school determines what collection costs are "reasonable," as long as they are based on actual costs the school incurs for the particular borrower, or on average costs incurred in collecting loans in similar stages of default. The school must be able to document the basis for the costs assessed. Schools may waive all or a portion of collection costs or make other compromises or consolidations based on a number of factors. The auditor should review Chapter Six of *The Student Financial Aid Handbook* applicable to the audit period to determine the conditions which apply.

The school may use a contractor for billing or collection, but the school is still responsible for complying with Subpart C regulations about those activities. For example, the school is still responsible for deciding whether to sue a borrower in default. A school may not use a billing service or a collection firm that owns or controls the other, or are owned or controlled by the same corporation, partnership, association, or individual.

Suggested Procedures

*[1]a. Review, evaluate, and document the institution's methodologies for determining compliance with Perkins collections and due diligence requirements.

b. Select a sample of Federal Perkins Loans which are representative of the loans in the schools portfolio and test their compliance with applicable SFA requirements. For example, for loans that have entered a grace period or repayment, determine that the proper number of contacts were made and that billing notices were appropriately given. Be aware at the grace periods and billing periods are measured in days not months or portions thereof. Verify that proper documentation exist for any deferments or cancellations.

1 *Review, evaluate and document means: the IPA must document his/her understanding of the relevant portions of the internal control structure and the assessed level of control risk.

SECTION III

PLANNING AND OTHER CONSIDERATIONS FOR AUDITS OF INSTITUTION SERVICERS

PURPOSE OF THIS SECTION

This section is to assist independent public accountants (IPAs) engaged to performed compliance attestation engagements of third-party service organizations [servicer(s)] when the functions performed are applicable to the administration of the U.S. Department of Education (ED) Federal Student Financial Assistance (SFA) Programs.

To the extent that an institution contracts with a servicer to administer any aspect of the SFA Programs, the applicable compliance requirements and guidance contained in other Sections of the Guide also apply to that servicer. This section must be used by the IPA to attest to the management assertions about compliance with the SFA programs made by any institution servicer participating in or administering any aspect of the SFA programs, except for institution servicers which obtain an audit in accordance with the Single Audit Act, OMB Circular A-133 or its predecessors. However, this Guide must be used if a program specific audit is being performed to satisfy the single audit requirements.

This guidance is not intended to be a complete manual of procedures, nor is it intended to supplant the IPA's judgment of the work required. Suggested procedures described may not cover all circumstances or conditions encountered. The IPA should use professional judgment and due care to tailor the procedures so that the compliance attestation engagement objectives are achieved. However, all applicable management assertions contained in this update must be addressed by the IPA. The IPA should contact the cognizant Regional Inspector General for Audit for technical assistance related to performing the engagement. (See Appendix C)

REQUIREMENTS AND STANDARDS FOR SERVICER ATTESTATION ENGAGEMENTS

Annual Compliance Audit

Section 487(c)(C)(I) of the Higher Education Act of 1965, as amended, (HEA) requires annual compliance audits of servicers with regard to any contract with an eligible institution, guaranty agency or lender for administering or servicing any aspect of the student financial assistance (SFA) programs. The HEA requires that these audits be performed in accordance with the U.S. General Accounting Office's *Government Auditing Standards*, issued by the Comptroller General of the United States. This Audit Guide provides guidance in satisfying the annual compliance audit requirement by performing an examination level attestation engagement of compliance and internal control over compliance under AICPA Statement on Standards for Attestation Engagements (SSAE) No. 3, Compliance Attestation.

Part 668.23 of Title 34 of the Code of Federal Regulations (CFR) requires that all servicers have an annual compliance audit performed of the servicer's administration of the participation in the Title IV, HEA programs of each institution with which the servicer has a contract, UNLESS:

--the servicer contracts with only one participating institution; and
--the audit of that institution's participation involves every aspect of the servicer's administration of that Title IV program.

SFA compliance attestation objectives are to determine and report whether the servicer management's assertions relative to compliance and internal control over compliance with specified compliance requirements in Section IV of this guide are fairly stated in all material respects (institutional eligibility and participation, reporting, student eligibility, disbursements, refunds, cash management, close out examinations, Perkins collections and due diligence, servicer eligibility, and servicer systems and internal controls).

ED in part meets its stewardship responsibilities by acting upon noncompliance and internal control weakness noted in the IPA's reports. Therefore, IPA's reports must contain adequate information to give reported matters perspective and to allow ED to take necessary corrective action.

These annual compliance audit requirements are considered satisfied by an audit conducted, where applicable, in accordance with the Single Audit Act, the Office of Management and Budget (OMB) Circular A-133, or its predecessors.

Standards for Servicer Attestation Engagements

The servicer's compliance attestation engagement shall be conducted by an independent auditor in accordance with the U.S. General Accounting Office's (GAO), *Government Auditing Standards (GAS)*, issued by the Comptroller General of the United States. ***This update requires an examination-level attestation engagement relative to a servicer management's assertions about certain compliance aspects related to SFA program participation as identified in Section IV. Therefore, in addition to applicable standards contained in the GAS, the Statement on Standards for Attestation Engagements (SSAE) No. 3, Compliance Attestation, issued by the American Institute of Certified Public Accountants (AICPA) also applies.*** An IPA engaged to perform a servicer compliance attestation engagement should also refer to Section I of this Guide for guidance concerning matters requiring immediate action, auditor qualifications, engagement letters, follow-up on prior audit findings, corrective action plan, quality control reviews, and future revisions as much of that guidance is not repeated in this section.

ENGAGEMENT PERIODS AND REPORT DUE DATES

First Year Engagements

A servicer's first engagement must cover the servicer's activities for the fiscal year, ending on or after July 1, 1996. Since regulations require audits for periods on or after July 1, 1994, in which the servicer administered any aspect of an institution's participation in the Title IV, HEA programs, ED reserves the right to request copies of audits for fiscal years prior to July 1, 1996.

Subsequent Engagements

Each subsequent annual engagement must cover the servicer's activities for the entire period of time (fiscal year) since the servicer's preceding engagement.

Due Dates

An institution's servicer shall submit its engagement report to ED within six months of the end of the servicer's fiscal year or, if applicable, in accordance with deadlines established in the Single Audit Act, OMB Circular A-133 or its predecessors. An institution's servicer's first engagement under this Guide must be submitted within six months after the issuance of this Section or six months after the end of the servicer's fiscal year, whichever is later.

A servicer's failure to meet report due dates may result in administrative sanctions described in 34 CFR 668, Subpart G.

SERVICER'S REPORTING ENTITY

Contracting With More Than One Institution, Lender or Guaranty Agency

A servicer that contracts with more than one participating institution may submit a single compliance attestation report that covers the applicable compliance requirements in Section IV of this Guide relating to the servicer's administration of the participation in the Title IV, HEA programs for each institution with which the servicer contracts.

A servicer that contracts with both an institution and a lender may not submit a single compliance attestation report to cover the servicer's participation in all of the Title IV, HEA programs. The servicer reports for lenders or guaranty agencies must be separate from the servicer audits for institutions because the services provided to each are markedly different.

SERVICER RESPONSIBILITIES

The servicer's management should assess the services it provides and whether it can make all or part of the applicable assertions in Section IV of this Guide. Scope limitations because of a servicer management's refusal to provide the applicable assertions may result in the servicer being subject to administrative actions listed in 34 CFR 668 Subpart G.

Servicer Corrective Action Plan

To assist in resolving instances of noncompliance, reportable conditions, and material weaknesses in the internal controls identified by the IPA, ED requires a servicer to develop a corrective action plan as part of its report. The corrective action plan is considered an essential part of the report requirement for the Title IV, HEA Programs. The corrective action plan is prepared by the servicer on the servicer's letterhead, and includes the name, title, and telephone number of the servicer official responsible for its preparation.

The corrective action plan must describe the corrective action taken or planned in response to findings identified by the IPA. In addition, the servicer must comment on the status of corrective action taken on prior findings. A suggested format for the corrective action plan is provided in Example H of Section V of this Guide.

PRACTITIONER RESPONSIBILITIFS

Engagement and Management Representations

The compliance attestation engagement must be performed as an examination-level engagement in accordance with SSAE No. 3 and *Government Auditing Standards*. The IPA is required to obtain written assertions from management as part of a compliance attestation engagement performed in accordance with SSAE No. 3. The nature of the written management assertions made by the servicer's management and the scope of the engagement may vary depending on the extent an institution has contracted with the servicer to perform certain compliance functions. Such assertions should be obtained from management in a letter of representation to the IPA. The letter of assertions should identify the services provided for which the servicer is responsible. The matrix in Example C-1 must be prepared and included as part of the reporting package.
All applicable management assertions contained in Section IV of the Guide must be addressed by the IPA. ***In addition to the specific assertions identified in that part, as applicable, management's written representations should include the matters required by paragraph 70 of SSAE No. 3.*** Paragraph 71 of SSAE No. 3 discusses the IPA's responsibility when management refuses to furnish all appropriate written representations.

PLANNING CONSIDERATIONS FOR SERVICER ATTESTATION ENGAGEMENTS

Purpose and Objective of Servicer Attestation Engagements

The overall purpose of the servicer engagements is to provide ED assurance that the servicer has complied with and has effective internal controls over the compliance requirements listed in Section IV of this Guide applicable to the servicer's administration of the participation in the SFA programs.

Consideration of the Servicer's Internal Controls

Overall guidance for the consideration of the internal controls and reporting requirements in an examination-level engagement is provided in *Government Auditing Standards* and in paragraphs 44-46 of SSAE No. 3. Paragraph 44 of SSAE No. 3 states that the practitioner should obtain an understanding of relevant portions of the internal controls over compliance sufficient to plan the examination engagement and to assess control risk for compliance with the specified requirements (that is, compliance requirements specified in Section IV of this guide). This guide further requires the practitioner to document his or her consideration of the servicer's policies and procedures and assessment of control risk. Section IV of this guide highlights the suggested procedures that have related internal control and risk assessment documentation requirements by the use of an "*".

During an examination-level attestation engagement, the IPA may become aware of reportable conditions or material weaknesses in the servicer's internal controls over compliance. A reportable condition is a significant deficiency in the design or operation of the internal controls over compliance that could adversely affect the servicer's ability to comply with the specified requirements. A material weakness is a reportable condition in which the design or operation of the internal controls does not reduce to a relatively low level the risk that noncompliance with one or more of the specified requirements could occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. The IPA's responsibility to communicate these deficiencies in an examination of management's assertion is similar to the IPA's responsibility described in SAS No. 60. However, this guide requires all communications of reportable conditions and material weaknesses in the internal controls over compliance to be in writing and requires the IPA to include a copy of such report(s) in the IPA's reporting package.

Except for reporting reportable conditions and material weaknesses as described above, no other reporting on the internal controls over compliance is required. The *Government Auditing Standards* requirement for a report on internal controls based on performing a financial-related audit does not apply.

Materiality

Paragraph 35 of SSAE No. 3 provides guidance on the IPA's consideration of materiality as it relates to each separate management assertion about compliance. Materiality for purposes of compliance assertions differs from materiality for financial reporting purposes. Accordingly, materiality relates to each separate management assertion about compliance. For the purposes of planning and performing tests for each of the compliance requirements, the IPA should consider the materiality of management's assertions in relation to each of the individual services performed. The IPA should issue a qualified or adverse compliance report when reporting instances of noncompliance that are material in relation to each of the specific compliance requirements.

This Guide requires that all instances of noncompliance pertaining to servicers be reported as a finding in the Schedule of Findings and Questioned Costs (see Reporting Noncompliance below). As discussed in paragraph 36 of SSAE No. 3, this should not change the practitioner's judgements about materiality in planning and performing the engagement or in forming an opinion on the servicer management's assertions.

Sampling Methodology

This guide requires sampling methodologies be used to test the required management assertions in Section IV for those assertions which apply to the servicer. The sample(s) must be taken randomly. In selecting a sample, consideration must be given to the systems used to provide services and the sample(s) must also include transactions that flow through all systems used by the servicer. The IPA must use professional judgment in determining the sample universes and sizes and that the sample relates to an audit objective. For example, if a servicer provides some clients with assistance in obtaining and maintaining their institutional eligibility, the IPA may consider taking a sample of the clients for whom this service is provided and evaluate compliance with Title IV regulations.

Sample Results

If the IPA determines that material noncompliance exists he/she must expand the sample in order to evaluate statistically the projected error rate and report total SFA questioned costs at the 95 percent confidence level with a confidence interval of $\pm 5\%$. Sample results must be considered in the context of either total SFA funding or individual attribute. Statistical sampling results must include information on the population, sample size, and error found in the sample.

All other noncompliance findings[1] must include information on the IPA's definition of material noncompliance, and the number of students and dollar value by school and by SFA program for:

- Population,
- Sample size, and
- Instances of noncompliance.

[1] During audit resolution ED may require a statistical sample or a full file review of all Title IV students to be completed.

Reporting Noncompliance

This Guide requires that all instances of noncompliance identified by the servicer's management in its assertions or by the IPA during the engagement must be reported as a finding in the Schedule of Findings and Questioned Costs. This applies even in those cases where corrective action was taken by the servicer after the examination period. The only exceptions are those instances of noncompliance that are detected by the servicer's internal controls and corrected in a timely manner.

Managements's assertions and the IPA's reports issued pursuant to this guide are a primary tool used by program managers in meeting their stewardship responsibilities in overseeing the SFA programs. The areas of noncompliance noted in management's assertions and/or the IPA's reports must be acted upon by ED program managers. To be of value, these reports must contain adequate information to give reported matters perspective and to allow the managers to take necessary corrective action.

If the report discloses material noncompliance (either in the servicer management's assertions or the IPA's report) or if immaterial noncompliance was identified by the servicer or the IPA during the engagement, the report or a separate communication must be sent to each institution serviced disclosing the instances of noncompliance applicable to the institution, and of management's plans to correct the noncompliance.

Compliance Attestation Reporting

The servicer shall transmit four copies of both the servicer's compliance reporting package and its corrective action plan to:

U.S. Department of Education
Office of Postsecondary Education
Institutional Participation & Oversight Service
Data Management & Analysis Division
600 Independence Avenue SW
ROB 3, Room 3082
Washington, D.C. 20202-5430

The servicer's report package must include the following:

1. Servicer Information Sheet (Example C-1);

2. A report on management's assertions on compliance with specified requirements applicable to SFA programs (Example D);

3. Schedule of Findings and Questioned Costs (Example F);

4. IPA's comments on resolution matters of prior audit findings (Example G);

5. Servicer's CAP (Example H);

6. Division of Responsibilities for Compliance Requirements (Example I);

7. If any, report on internal control over compliance of any reportable conditions or material weaknesses noted in accordance with SSAE No. 3 paragraph 46;

8. If a separate report on illegal acts which could result in criminal prosecution was submitted in accordance with the instructions in Section I of this guide, it should also be included as part of the reporting package; and

9. If separate communications are sent to each institution disclosing the impact of the findings on the institutions, those communications should also be included as part of the reporting package.

SECTION IV

REQUIRED SERVICER MANAGEMENT ASSERTIONS, COMPLIANCE REQUIREMENTS, AND SUGGESTED PROCEDURES

INTRODUCTION

This section:

1. Sets forth the minimum standards, which are the subject of management's written compliance assertions;

2. Briefly describes the related compliance requirements; and

3. Provides guidance on the general approach the IPA should consider in designing and carrying out procedures in the examination of management's written assertions.

As discussed in Sections I and III of the Guide, the suggested procedures in Sections II and IV of the Guide are not intended to be a complete set of procedures to satisfy the engagement objectives, nor are they intended to supplant the IPA's judgment about the testing necessary for the IPA to report on management's assertions. Also, management's assertions may need to be modified based on the services performed.

To perform the engagement, the IPA should obtain, read, and/or have available:

- 34 CFR Parts 600, 668, 674, 675, 676, 682, 685, 690 (Contained in 34 CFR Part 400 To End, revised as of *July 1, 1996 and final regulations issued for 34 CFR Parts 668, 673, 674, 675, 676 and 690 on November 27, 1996; Parts 600 and 668 on November 29, 1996; and Parts 668, 674, 675, 676, 682, 685, and 690 on November 29, 1996;*

- ED "Dear Colleague" letters;

- The Direct Loan School Guide for the year(s) being audited; and

- The servicer's client contracts and the following documents for each of its clients

  - Federal Cash Transaction Report PMS 272 or, as appropriate, the ED/PMS 272, Federal Cash Transactions Report - Status of Federal Cash and ED/PMS 272a, Federal Cash Transactions Report.
  - Monthly Cash Summary and Data Matching Reconciliations for FDLP
  - Student Status Confirmation Reports (SSCRs)
  - Final Student Payment Summary (SPS)

The IPA should be familiar with the relevant statutes and sections of the CFR to obtain a complete understanding of the compliance requirements. Specific requirements may change periodically. IPAs should be alert to those changes. An excellent resource for updated SFA information is the annual Federal Student Financial Aid Handbook.

1. INSTITUTIONAL ELIGIBILITY AND PARTICIPATION

Required Management Assertion

[Servicer] complied with the Institutional Eligibility and Participation compliance requirements listed in Section II of the ED SFA Guide as applicable to our clients.

Compliance Requirements and Suggested Procedures

Servicers may contract to assist institutions to obtain and/or maintain their eligibility to participate in the Title IV, HEA programs. The institutional eligibility and participation compliance requirements are discussed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided. To the extent that the servicer contracts to assist an institution in obtaining and/or maintaining its eligibility, the auditor should review the requirements and perform the suggested procedures in Section II.

2. REPORTING

Required Management Assertion

[Servicer] complied with the Reporting requirements, [list reports], listed in Section II of the ED SFA Guide as applicable to our clients.

Compliance Requirements and Suggested Procedures

Servicers may contract to provide financial and student record maintenance for institutions which will include compliance with reporting requirements as discussed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services and reports are to be provided. To the extent that the servicer contracts to comply with any of the reporting requirements, the auditor should review the requirements and perform the suggested procedures in Section II.

3. STUDENT ELIGIBILITY

Required Management Assertion

[Servicer] complied with the Student Eligibility compliance requirements listed in Section II of the ED SFA Guide as applicable to our clients.

Compliance Requirements and Suggested Procedures

SFA program descriptions and compliance requirements are detailed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provide with regard to the determination of student eligibility and the related compliance requirements. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with student eligibility. The sample of student files to test will be based on the sampling methodology discussed in Section III. The determination that a student's financial aid award is not in excess of their need (suggested procedure c. 8 on page II-12) is the determination that the award is accurate and does not exceed any applicable aggregate or annual limits. Tests should be based on information available at the servicer, either electronic files or hard copies, and there should be no need to obtain student files or award packages from institutions.

4. DISBURSEMENTS

Required Management Assertion

[Servicer] complied with the Disbursements compliance requirements listed in Section II of the ED SFA Guide as applicable to our clients.

Compliance Requirements and Suggested Procedures

SFA compliance requirements, including payment periods, credit balances in student accounts and disbursement criteria are detailed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided with regard to the disbursement of SFA funds and the related compliance requirements. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with disbursements. The sample of student files to test will be based on the sampling methodology discussed in Section III. Caution should be exercised when the servicer writes award checks. In these cases, the auditor should document the procedures used to actually disburse the funds, who signed the checks, procedures to ensure that the student attended classes for the prescribed time prior to the disbursement of the funds, and the return of funds when appropriate. Tests should be based on information available at the servicer, either electronic files or hard copies, and there should be no need to obtain student files or award packages from institutions.

5. REFUNDS

Required Management Assertion

[Servicer] complied with the Refund compliance requirements listed in Section II of the ED SFA Guide as applicable to our clients.

Compliance Requirements and Suggested Procedures

SFA compliance requirements, including refund sequence, time frame for return of Federal funds, and leave of absence withdrawals are detailed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided with regard to refunds. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with refunds. The sample of student files to test will be based on the sampling methodology discussed in Section III. The determination that the proper refund has been calculated and made within the due dates and in the proper sequence should be based on the information available at the servicer, either electronic files or hard copies, and there should be no need to obtain student files from institutions.

6. CASH MANAGEMENT

Required Management Assertion

[Servicer] complied with the Cash Management compliance requirements listed in Section II of the ED SFA guide as applicable.

FOR FISCAL YEARS ENDING THROUGH JUNE 30, 1995, THIS COMPLIANCE REQUIREMENT APPLIES ONLY TO SERVICERS THAT REQUESTED MORE THAN $1,000,000 OF TITLE IV FUNDING DIRECTLY FROM ED FOR ITS CLIENTS.

FOR FISCAL YEARS ENDING BETWEEN JULY 1, 1995, AND JUNE 30, 1996, THIS COMPLIANCE REQUIREMENT APPLIES ONLY TO SERVICERS THAT REQUESTED MORE THAN $500,000 OF TITLE IV FUNDING DIRECTLY FROM ED FOR ITS CLIENTS.

FOR FISCAL YEARS STARTING ON OR AFTER JULY 1, 1996, THESE COMPLIANCE REQUIREMENTS APPLIES ONLY TO SERVICERS THAT REQUESTED MORE THAN $300,000 OF TITLE IV FUNDING DIRECTLY FROM ED FOR ITS CLIENTS.

Compliance Requirements and Suggested Procedures

SFA compliance requirements are detailed in Section II of this Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided with regard to cash management and the related compliance requirements and their applicability. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with cash management. The cash management rules and procedures that apply to an institution under 34 CFR 668 Subpart K also apply to a third-party servicer. The auditor should document the servicer's cash management responsibilities. Particular care should be given to the servicer's procedures for ensuring that funds drawn are disbursed within three working days and that excess cash tolerances are not exceeded.

7. CLOSE OUT (IF APPLICABLE)

If an institution loses its eligibility, ceases to provide educational instruction, or discontinues participation in the Title IV program during the award year, the following additional compliance requirements must be tested. Further, other compliance requirements in this audit guide must be tested.

Required Management Assertion

[Servicer] complied with Close Out compliance requirements listed in Section II of the ED SFA Guide as they apply to our clients.

Compliance Requirements and Suggested Procedures

SFA compliance requirements are detailed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided with regard to an institution which ceases to participate in the Title IV programs during the award year and the related compliance requirements and their applicability. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with close out. The auditor should document the servicer's responsibilities for any of its clients which may have ceased participation in the Title IV program during the award year. Particular care should be given to if and how the servicer assists the closed client in its arrangements with regard to records concerning the administration of the program and, if applicable, the collection of any outstanding Perkins or FDLP loans.

8. PERKINS LOAN COLLECTIONS AND DUE DILIGENCE

Required Management Assertion

[Servicer] complied with the Perkins Collections and Due Diligence compliance requirements listed in Section II of the ED SFA Guide as they apply to our clients.

Compliance Requirements and Suggested Procedures

SFA compliance requirements concerning Perkins Collections and Due Diligence are detailed in Section II of the Guide. The auditor should review the servicer's contracts with its clients to obtain an understanding of what services are to be provided with regard to collections and due diligence over Perkins funds and the related compliance requirements. Based on the services provided, the auditor should perform the suggested procedures in Section II dealing with collections and due diligence. However, the sample of student files to test should be based on the sampling methodology discussed in Section III.

9. SERVICER ELIGIBILITY

Required Management Assertion

[Servicer] complied with the Third-Party Eligibility compliance requirements listed in Section IV of the ED SFA Guide.

Compliance Requirements

An institution may enter into a written contract with a third-party servicer only to the extent that the servicer's eligibility has not been limited, suspended or terminated under the proceedings of 34 CFR 668 Subpart G.

- A third-party servicer may not enter into a written contract with an institution if the servicer has:
    - Been limited, suspended, or terminated by the Secretary within the preceding five years;
    - Had, during the two most recent audits, a finding that resulted in the servicer being required to repay an amount greater than five percent of the funds that the servicer administered under the Title IV programs for any award year; or
    - Been cited during the preceding five years for failure to submit required audit reports in a timely fashion.
    - Been subjected to a termination action and either the servicer, or one or more persons or entities that exercise substantial control over the servicer, or both:
        - failed to submit financial guarantees in an amount determined to be sufficient to satisfy potential liabilities arising from the servicer's administration of the Title IV, HEA programs; and
        - failed to agreed to be jointly or severally liable for any liabilities arising from the servicer's administration of the Title IV, HEA programs and the civil and criminal monetary penalties authorized under Title IV of the HEA.

- In a contract with an institution, a third-party servicer shall agree to:
  - Comply with all statutory or regulatory provisions, and special arrangements, agreements, limitations, suspensions, and terminations entered into under Title IV HEA Programs.
  - Refer to the Office of Inspector General of ED for investigation any information indicating there is reasonable cause to believe:
    - the institution might have engaged in fraud or other criminal misconduct in connection with the institution's administration of any Title IV, HEA program, or
    - an applicant for Title IV, HEA program assistance might have engaged in fraud or other criminal misconduct in connection with his or her application.
  - Be jointly and severally liable with the institution for any violation by the servicer of any statutory or regulatory provisions, and special arrangements, agreements, limitations, suspensions, and terminations entered into under the Title IV HEA Programs.
  - In the case of a servicer that disburses funds or delivers FFELP proceeds to a student:
    - Confirm the eligibility of the student before making that disbursement or delivering those proceeds; and
    - Calculate and pay refunds and repayments due a student, the Title IV, HEA program accounts, and the student's lender under the FSLP, Federal PLUS and Federal SLS programs in accordance with the institution's refund policy, the provisions of Sec.668.21 and Sec. 668.22, and applicable program regulation.
  - If the contract is terminated, or the servicer stops providing services, goes out of business, or files a petition under the Bankruptcy Code, return to the institution all:
    - Records in the servicer's possession pertaining to the institution's participation in the program or programs for which services are no longer provided; and

- Funds, including Title IV, HEA program funds, received from or on behalf of the institution's students, for the purposes of the program or programs for which services are no longer provided.

The IPA should immediately notify the servicer and/or its governing body if it is determined that the servicer fails to meet any servicer eligibility criterion. The IPA should follow the guidance for reporting irregularities and illegal acts as discussed in Section I of the Guide.

Suggested Procedures

a. Make inquiries of the servicer's management and obtain, as part of the management representation, written representation that the servicer has not:

   1. been limited, suspended, or terminated by the Secretary within the preceding five years; and

   2. had to repay an amount greater than five percent of the funds it administered under the Title IV programs for any award year as a result of a finding in one of the two most recent audits; and

   3. been cited for failure to submit required audits during the preceding five years.

b. Review a representative sample of the servicer's contracts to determine if the servicer has agreed to comply with the requirements contained in 34 CFR 668.25(c), concerning compliance, referrals and liability.

10. SERVICER'S SYSTEMS AND INTERNAL CONTROLS

Required Management Assertion

[Servicer] has established systems with internal controls which assured compliance with requirements listed in Section II of the ED SFA Guide for those services which it provided.

Compliance Requirements

In addition to examining the servicer management's assertions about the specified compliance requirements identified in Section II, this guide also requires the practitioner to examine and report on the servicer management's assertion about the effectiveness of the servicer's internal control structure over compliance with those specified compliance requirements.

Management is responsible for the effectiveness of the servicer's internal control structure and for evaluating its effectiveness using reasonable criteria. As discussed in paragraph 6 of SSAE No. 3, practitioners are allowed to accept an engagement to examine management's assertion about the effectiveness of the entity's internal control structure over compliance only if management uses reasonable criteria, such as those established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). When the servicer uses computers to process data the auditor may find useful information in the General Accounting Office publication *Assessing the Reliability of Computer-Processed Data* (GAO/OP-8.1.3, September 1990).

In performing the examination-level engagement, the practitioner is required to obtain an understanding of the relevant portions of the servicer's internal control structure over compliance as described above, and to test and evaluate the design and operating effectiveness of the servicer's internal control structure over compliance with those specified compliance requirements. As the internal control structure over compliance varies among servicers, not all of the suggested procedures below may be applicable for testing the design and operating effectiveness of the servicer's internal control structure over compliance.

A servicer should have controls, however, that give the servicer reasonable assurance that it is complying with the specified compliance requirements identified in Section II of this guide. Thus for purposes of management and practitioner reporting, the severity of control deficiencies relates to whether those internal controls prevent or detect material noncompliance in each of the specified areas. Overall guidance for the consideration of the internal control structure and reporting requirements in an examination-level attestation engagement is provided in paragraphs 44-46 of SSAE No.3.

Suggested Procedures

a. Document the system of internal controls over each SFA program service provided. This may consist of flowcharts, narratives or checklists, but must present a clear understanding of the servicer's systems and its controls.

b. Select a sample of transactions which are representative of the functions preformed and test their accuracy and compliance with applicable SFA requirements. For example, if Pell awards are determined by the servicer, the sample should include a number of student records and the computed awards. From the information available at the servicer, either electronic or hard copy files, evaluate the accuracy of the data and recompute the Pell awards. Be aware of possible inconsistencies in the data.

c. In those cases where the servicer uses automated systems, consideration should be given to developing and running a "test deck" or other procedures on the servicer's automated systems to insure that they function in accordance with documented procedures. The procedures should also be reviewed to determine that they comply with applicable SFA regulations.

EXAMPLE B-1

REPORT PACKAGE COVER PAGE

NAME OF SERVICER

CITY, STATE

COMPLIANCE ATTESTATION EXAMINATION
OF THE TITLE IV STUDENT FINANCIAL ASSISTANCE PROGRAMS

FOR THE FISCAL YEAR ENDING MONTH/DAY, YEAR

XYZ & Co.
Certified Public Accountants

EXAMPLE C-1

SERVICER INFORMATION SHEET

NAME OF SERVICER
SERVICER ADDRESS

TEL. NO. (____) _____ -_____
FAX. NO. (____) _____ -_____
PRESIDENT: _____
CONTACT PERSON & TITLE: _____

LEAD AUDITOR: _____
FIRM'S NAME: _____
ADDRESS: _____
_____
_____

TEL. NO. (____) _____ -_____
FAX. NO. (____) _____ -_____

DIVISION OF RESPONSIBILITY FOR COMPLIANCE REQUIREMENTS

Compliance Requirement	*Responsibility of Institution*	*Responsibility of XYZ Service Center*	*Explanation of Divided Responsibility*
I. Computer operations			
A. Terminal and software security			
B. Data integrity			
C. System and data backup			
D. Disaster recovery plan			
II. Cash management			
A. Drawdowns			
B. Authorization vs. expenditures			
C. Reconcile G/L to bank			
D. Bank account notes federal funds			
III. Financial reports			
A. FISAP			
B. EDPMTS/EDCAPS			
C. Pell IPS			

EXAMPLE C-1

Compliance Requirement	*Responsibility of Institution*	*Responsibility of XYZ Service Center*	*Explanation of Divided Responsibility*
IV. Institutional eligibility			
A. Participation agreement/ECAR			
B. Accreditation status			
C. Admissions policy			
D. Eligible programs			
E. Calculation of institution eligibility ratios			
F. Licenses			
G. Administrative capability items			
V. Student eligibility			
A. High school diploma or equivalent or ability to benefit			
B. Regularly enrolled in eligible program			
C. Citizen or permanent resident			
D. Satisfactory progress			
E. Default/refund status			
F. Social security number match requirement			
G. Other requirements			
VI. Coordination of programs			
A. Financial aid organization			
B. Other information available			
C. Needs analysis			
D. Professional judgement documentation			
VII. Administrative capability			
A. Student file maintenance			
B. Record retention			
C. Verification			
VIII. Disbursements			
A. Financial aid transcripts/NSLDS information			
B. Independent/Dependent status determination			
C. Timing and amount of disbursements			
IX. Refunds or overpayments			
A. Policy			
B. Refund calculations			
C. Overpayment calculations			
D. Disbursement and accounting for refunds/overpayments			

EXAMPLE C-1

Compliance Requirement	*Responsibility of Institution*	*Responsibility of XYZ Service Center*	*Explanation of Divided Responsibility*
X. Institutional disclosure			
A. Accuracy of institutional data			
B. Disclosure to students			
XI. Pell grant			
A. Types of expenditures allowed			
B. Program performance			
1. Calculation and disbursement of award			
2. Timing of payment; cutoff dates for receipts of SARs			
C. Financial reports			
XII. Campus-based programs (general)			
A. Types of expenditure allowed			
1. Program expenditures			
2. Administrative cost allowance			
B. Program performance			
1. Accuracy of FISAP data			
2. System of need analysis, etc.			
XIII. Campus-based programs (Perkins)			
A. Type of expenditures allowed			
B. Matching			
C. Program performance			
1. Student eligibility			
2. Approved promissory note			
3. Due diligence			
4. Repayment records			
D. Special compliance requirements			
1. Minimum cash balance; cash planning			
2. Treatment of interest earned on Perkins loan balance			
XIV. Campus-based programs (FSEOG)			
A. Eligible expenditures			
B. Matching			
C. Selection of students for FSEOG awards			

EXAMPLE C-1
Page 4 of 4

Compliance Requirement	*Responsibility of Institution*	*Responsibility of XYZ Service Center*	*Explanation of Divided Responsibility*
XV. Campus-based programs (FWS)			
A. Types of expenditures and employment allowed			
1. Types of employment allowed			
2. Types of expenditures allowed			
B. Matching			
C. Program performance			
1. Selection of students for employment			
2. Approval of time sheets and payment to students			
D. Special compliance requirements			
1. JLD and CSJLD programs			
2. CSL programs (5% minimum)			
XVI. Federal Family Education Loans (FFEL)			
A. Program performance			
1. Determination of eligibility and completion of application			
2. Default reduction measures			
3. Entrance and exit counseling			
4. Loan disbursement			
5. EFT Roster reconciliation			
6. Eligibility for disbursement			
B. Status reporting			
1. SSCR completion			
2. Change in enrollment status			
C. Special compliance requirements			
1. Refund policy			
2. Refunds to lenders			
XVII. Federal Direct Loan Program (FDLP)			
A. Program performance			
1. Determination of eligibility			
2. Entrance and exit counseling			
3. Exporting & importing electronic files to/from the LOC			
4. Loan disbursement			
5. Monthly data matching including:			
1. Loan and cash detail records			
2. Summary records			
B. FDLP status reporting			
1. SSCRs			
2. Change in enrollment status			

APPENDIX D

INSTRUCTIONS FOR EXAMPLE E

Example E, Schedules A, B and C may be submitted on either diskette or on paper. If there are no finding concerning specific students, these schedules are not required.

Diskette Submission

To submit Example E, Schedules A, B and C by diskette you need Internet access (either by modem or through a LAN). The program files have been consolidated into a single file - SFASCHED.EXE to facilitate downloading. SFASCHED.EXE can be downloaded from the Nonfederal team's Internet website at the URL (use lower case): http://home.gvi.net/~edoig/ Proceed to the section titled SFA Audits - Specific Guidance, go down until you see: Software for Generating Schedules A, B, C. Click on that title and follow the downloading instructions.

Minimum requirements for utilizing SFASCHED.EXE include:

An IBM compatible computer with a 286 microprocessor
2 MB of RAM (1MB must be extended memory)
A Hard Disk with a minimum of 2 MB free space
Printer (Hewlett-Packard LaserJet recommended or a dot matrix printer capable of printing in pica and elite pitch [10/12 cpi])
DOS 3.3x or above

NOTE: If using Windows, exit to DOS (to root directory C:\) to run the program.

Paper Submission

To keep from violating the Privacy Act, Schedules A, B and C submitted by paper must NOT include the student's name or social security number. You must assign each student from each sample a specific number (identical to the software above, the number assigned must contain a suffix which identifies from which universe of students the student was selected, i.e. the suffix "a" for the universe of students who did not drop, withdraw or terminate, the suffix "b" for the universe of students who did drop, withdraw or terminate) and list that number on the appropriate schedule. A separate document must be submitted with the audit report package that identifies each student by their specific number, name, and social security number. This separate document CANNOT be bound in the audit report package.

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